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SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1959

No. 676

IN THE MATTER

116TH STREET PAWNBROKERS, INC.,

Bankrupt

RICHARD SHONGUT, JACOB SHONGUT, INC. and MITCHELL McGRAW,

Petitioners-Appellants

v.

JULES GOLDEN,

Trustee-Respondent

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

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OCTOBER TERM, 1959

No. .....

IN THE MATTER

of

116TH STREET PAWNBROKERS, INC.,
Bankrupt.

RICHARD SHONGUT, JACOB SHONGUT, INC. and MITCHELL MOGAL,
Petitioners-Appellants.

JULES GOLDEN,
Trustee-Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

The petitioners hereby pray that a writ of certiorari issue in the above entitled proceeding to review the judgment of the United States Court of Appeals for the Second Circuit, entered in the above entitled proceeding on September 9, 1959.

Citations to Opinion Below

The memorandum opinion of the Referee in Bankruptcy (record p. 157), is unreported, and is printed in Appendix to the Record (p. 49a). The opinion of the District Court

(Record p. 190) is unreported and is printed in the Appendix to the Record (p. 10a). The opinion of the Court of Appeals, infra p. 15, is reported in 270 F. 2nd 238.

Jurisdiction

The judgment of the Court of Appeals was entered on September 9, 1959 (Appendix p. 57a). Extension of time in which to file a petition for writ of certiorari until February 5, 1960, was granted by Mr. Justice John M. Harlan on December 8, 1959. The jurisdiction of this Court is invoked under 11 U. S. C., Sec. 47(c) and Sec. 24(c) of the Bankruptcy Act.

Question Presented

Whether a plan of arrangement under Chapter XI of the Bankruptcy Act was refused through the efforts and at the cost and expense of the petitioners herein.

Statute Involved

The statutory provision involved is Sec. 64(a)(3) of the Bankruptcy Act, 11 U. S. C., § 104(a)(3). It is printed in Appendix p. 48a.

Statement

The 116th Street Pawnbrokers, Inc., on December 14, 1955, filed a petition for a plan of arrangement pursuant to Chapter XI of the Bankruptcy Act. Several amendments of the plan were thereafter filed by the debtor. On March 8, 1956, the debtor filed its third amended plan of arrangement (App. p. 40a). On May 8, 1956, a hearing in connection with the third amended plan was had before the Referee in Bankruptcy. It was then announced that a majority of the creditors, in numbers and amounts, had approved the plan. The appellants—the only three object-

ing creditors—opposed it. They had, in fact, been the only creditors who had opposed from the outset any plan of arrangement. The Referee directed that specifications of objections be filed by appellants on or before May 22, 1956; and further that upon such filing, the hearing on the objections would be held on May 31, 1956.

On May 8, 1956, at that same hearing, the debtor made application for permission to borrow $10,000.00, which the Referee granted (App. p. 45a).

The appellants within the prescribed time filed their specifications of objections, and paid $20.00 for filing fees.

Thereafter, on May 23, 1956, the Referee in Bankruptcy sent notices to the attorneys for the appellants and to the attorney for the debtor that, pursuant to Rule XI-8 of the Bankruptcy Rules, the appellants, as objectors to the confirmation of the plan of arrangement, were required to deposit on or before May 29, 1956, the sum of $50.00 each, to pay the expenses of the Court stenographer in reporting the minutes of the hearing, with the further proviso that if such deposit were not then made, the objections might be dismissed (App. p. 46a).

Within the time permitted, the appellants deposited with the Referee's stenographer, the said sum of $100.00.

On May 31, 1956 there appeared on the Referee's calendar, two matters:

1. Hearing on specifications of objections filed by appellants.

2. Hearing on confirmation of plan of arrangement.

When the hearing on the objections was called by the Referee on May 31, 1956, he stated that, since there were three objectors, and having only received $20.00 as his fees, that it would be necessary that an additional $10.00 be paid to him for the third objecting creditor before he would hear the objections. The additional $10.00 was promptly paid to and accepted by the Referee.

The objectors indicated that they were then ready to present their proof, and called their first witness.

The attorney for the debtor then sought to withdraw the plan of arrangement. The Referee denied such application.

The attorney for the debtor interrupted the proceedings, and without prior notice, stated to the Referee that no deposit was made by the debtor. The Referee thereupon refused to hear the proof which appellants were ready to offer in support of their specifications of objections, and, instead, adjudicated the debtor a bankrupt.

On August 8, 1957, ABRAHAM J. GOLDBERG, the attorney for the appellants RICHARD SHONGUT and JACOB SHONGUT, INC., petitioned the Referee for an allowance pursuant to Section 64a (3) of the Bankruptcy Act. A similar petition was filed by Solomon Nachbar, the attorney for appellant, MITCHELL MOGAL.

On September 12, 1957 at a hearing before the Referee, the petitions of the attorneys for the appellants were dismissed with leave to renew upon separate petitions to be filed by the appellant creditors.

On November 26, 1957 JACOB SHONGUT, INC. and RICHARD SHONGUT, two of the appellants herein, filed a joint petition for an allowance. A similar petition was filed by the appellant, MITCHELL MOGAL, on December 6, 1957. A hearing thereon was held by the Referee on January 30, 1958. The Referee, however, refused to consider the petitions at that time and required that supplemental separate petitions be filed by each of the appellants.

On February 19, 1958, appellants filed separate supplemental petitions.

The Referee requested the attorneys for the petitioners and respondent to file additional affidavits. On March 11, 1958, such additional affidavits were filed.

On March 14, 1958, a hearing was had before the Referee.

On March 23, 1958, the Referee filed his Opinion dismissing the petitions of appellants for allowance pursuant to Section 64a (3) of the Bankruptcy Act (App. p. 49a).

On April 3, 1958, the Referee signed an order dismissing the petitions.

On April 14, 1958, the appellants filed a petition for review to the District Court of the Southern District of New York.

A hearing was had before the Hon. Sidney Sugarman on May 2, 1958.

On July 19, 1958, the Hon. Sidney Sugarman affirmed, without opinion, the order of the Referee dismissing the petitions for allowance pursuant to Section 64a (3) of the Bankruptcy Act.

On August 28, 1958, appellants served and filed their notices of appeal from the order of the District Court, which affirmed the order of Referee Robert P. Stephenson.

The Court of Appeals, Second Circuit, affirmed the order of the District Court on September 9, 1959.

Jurisdiction in the Court of Appeals was pursuant to Section 24a of the Bankruptcy Act.

Jurisdiction of the District Court was pursuant to Section 2 of the Bankruptcy Act.

Reasons for Granting Writ

1.

The question as to the rights of an objecting creditor in a proceeding under Chapter XI of the Bankruptcy Act, for reimbursement for costs and expenses in opposing an application for confirmation of a plan of arrangement has never before been presented to this Court. It is of sufficient general application beyond the interests of the parties to this proceeding.

The Court below held that there was no refusal of confirmation and that the denial of the allowances sought by these appellants was proper.

The Court erred in its reasoning and in its decision. It overlooked the significance of the fact that once a plan of arrangement had been accepted by a majority of the creditors, in numbers and amounts, it could not be withdrawn directly or indirectly. *In Re Bryer*, 281 Fed. 812. This is particularly so, where, as here, specifications of objections to the plan of arrangement had been filed, and a hearing scheduled. If a plan may not be directly withdrawn, it cannot be done through the guise of "not making a deposit." Had the Court considered the facts, it would have found that on the very day that the hearing on the objections was held (May 31, 1956), the debtor had cash in the bank and on hand of some $8,000. In addition, the Court had only on May 8, 1956 approved a loan for $10,000. The total amount of the deposit required could not have exceeded $1,800.*

Under the plan of arrangement it was not necessary for any immediate payment to creditors or administration claimants. The only deposit that was required was for payments to the referee's salary and expense funds, and miscellaneous administration expenses. There were sufficient funds available towards such a deposit.

It is submitted that if the decision of the Court of Appeals is to be the prevailing law, then no diligent creditor would incur expenses to oppose a plan of arrangement. For, to hold—as the Court did—that the adjudication was not a "refusal" of confirmation due to the efforts of the appellants, debtor, in any case, can thwart the opposition of a diligent creditor by stating, at the last moment, that he *cannot* make the deposit.

The Court held "For throughout the Act reference to a *refusal* of confirmation imports a refusal based on lack of merit in the plan in contradistinction from lack of the ful-

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* See 3rd Amended plan, App. p. 40a.

fillment of the several stated procedural conditions to confirmation." (App. p. 54a) It erroneously stated " . . . it is not permissible to argue that the confirmation was 'refused' because of lack of application and deposit." It disregarded the finding of the Referee:

> "When the hearing on objections was called, the debtor tried to withdraw its arrangement. This was not permitted as it could not be withdrawn after acceptance. It then appeared that the debtor had not made the deposit required." (App. p. 49a)

Can it be said, as the Court held, that it is "not permissible to argue that the confirmation was refused because of lack of . . . deposit." The Referee recognized that the debtor sought to withdraw its plan but based his finding upon the fact that having failed to make the deposit, the plan of arrangement could not be confirmed.

Considering that if on May 31, 1956, the debtor had made the deposit required, the appellants would have been obliged to proceed immediately with the hearing on the objections. It is an anomaly to say that a creditor who, on the one hand must be prepared to proceed with his objections, should not incur any expense until it is first determined whether the debtor will make the deposit.

When the referee set May 31, 1956 as the date for the hearing on the objections, he did so with full knowledge of the facts.

He required appellants to bear the cost of filing the objections and the cost of the stenographic minutes (App. p. 46a). At the hearing on the objections, he demanded and accepted an additional $10.00 filing fee from the appellants.

The hearing on the objections had *begun*.

The question of the attempted withdrawal of the plan and the statement by the debtor that no deposit had been made, did not arise until after the hearing had begun. The

debtor made no reference to his failure to make the deposit until after the referee had ruled that there could be no withdrawal of the plan.

When the referee denied the application of the debtor to withdraw his plan, the referee did so in accordance with *In Re Bryer*, 281 Fed. 812, 813. There the court held that a plan of arrangement, once accepted, could not be withdrawn.

> " . . . an objecting creditor or creditors may have incurred the expense of opposition, and their counsel may have taken appropriate proceedings to present facts which, if found against the bankrupt, may operate later as a bar to his discharge."

Jacob I. Weinstein, a member of the National Bankruptcy Conference, in discussing objections raised by those who opposed reimbursement of costs to objecting creditors, set forth his reasons in favor of reimbursement at the Congressional Hearings at H. R. 6439, 75th Congress, First Session (1937), p. 162 as follows:

> " . . . and it was necessary if there was to be any interest aroused, to provide, that when the creditors undertook the inquiry and they produced actual results . . . if they succeed in obtaining a refusal of a confirmation of an arrangement . . . then the court may, in its discretion allow that expense in connection with that service."

Congress went much further than suggested by Mr. Weinstein. It eliminated that part that made the reimbursements of costs and expenses discretionary. [*Chandler Act*, Sec. 64a(3).] By making it mandatory, Congress wished to encourage creditors in making investigations.

Collier on Bankruptcy, Vol. 3, 14th Ed. p. 2105, following the reasoning of Mr. Weinstein states: "Despite the language of § 64a(3) it is thought that the provision does not preclude allowance and priority costs and expenses incurred

in successfully opposing the mere offer of an arrangement or plan."

In the nature of things, creditors must make an investigation to determine whether it appears that facts exist to form the basis of objecting to a plan of arrangement under Chapter XI of the Bankruptcy Act. They cannot and must not wait until the last moment when proper preparation is impossible. Fraud or feasibility are factors which must be considered, and can be determined only *after* a preliminary investigation.

These are the very factors that the lower Court disregarded when it stated that creditors intending to incur expenses in opposing a plan could have "pressed" the Referee to set a time limit within which the debtor might apply for confirmation, and to set the hearing on confirmation at a later date, in order to permit suitable preparation for the hearing. The appellants made preliminary investigation prior to May 8, 1956 to determine if they would approve or oppose the plan. Their preliminary investigation showed grounds for opposing the plan. It was on that date when the majority of the creditors approved the plan that, based upon the preliminary investigations, appellants stated that they were prepared to file the objections. It was the Referee* who then set the time schedule. Between May 8, 1956 and May 22, 1956 when the specifications of objections were filed, appellants had, of necessity, to make further investigation in order to be prepared properly. To say that appellants should not have done anything until it was determined that the debtor would make his deposit, is begging the question. For all intents and purposes when the creditors on May 8, 1956 approved the plan, the debtor fully intended to carry it out. The debtor then applied to the Referee, for permission to borrow $10,000. That appli-

* Referee Robert P. Stephenson has been an official Bankruptcy Referee for more than 30 years. When he set the time schedule it was based on his long experience in these matters.

cation, over the objection of the appellants, was granted. It was further proof that the debtor fully intended to carry out the plan.

After the objections were served and filed on May 22, 1956 the debtor had one week to examine the objections. An effort was made by the debtor to have appellants withdraw their objections (App. p. 28a). When it was apparent that appellants would not withdraw the objections and fully intended to proceed, the debtor knowing that the objections would be sustained, then for the first time, stated that no deposit had been made. By use of this procedural "trick", the debtor accomplished indirectly what it could not do directly.

The refusal to confirm was not based on the non-fulfilment of the procedural conditions, as indicated by the court. It was based on the merits of the case. "Refusal" may be in various forms, and may be inferred from the circumstances surrounding the proceedings.

An adjudication in bankruptcy and a refusal to confirm are two distinct matters. Appellants contend that adjudication was not a factor to be considered at the hearing on objections on May 31, 1956. The only matter called for hearing was on the objections filed by the appellants.

2.

When appellants filed their objections, they were in the nature of plaintiffs to a new proceeding. The objections must first be heard. This the Referee did not and would not do.

This court, in *Myers* vs. *International Trust Company*, 263 U. S. 64, 72, held that a reference to a referee for a hearing of objections to a confirmation of a plan of arrangement is equivalent to a hearing in equity. It constitutes the beginning of a distinct, separate and new suit. At the hearing on the objections, the Referee could determine whether the plan of arrangement should be "confirmed" or

"refused." Only after he had decided to "refuse" to confirm the plan could he consider the question of dismissal or adjudication. It cannot be stressed too strongly at this time that "refusal" and "adjudication" are two different facets of the Bankruptcy Act. The Court below could not use the factor of "adjudication" to decide the question of "refusal".

It has always been the position of the courts that substance rather than form should govern. The Court below erred in stressing only the "form" which the proceedings took on May 31, 1956, instead of the "substance" of the matter. In *Continental Insurance Co.* vs. *Louisiana Oil Refining Corp.*, 89 F. (2nd) 333, 338, the Court of Appeals of the 5th Circuit stated that the "judge should have looked beyond its *form* to its *substance* and have inquired into it instead of rejecting it as without effect." (italics ours).

3.

Clearly the question presented is of importance in the administration of the Federal Bankruptcy Act. Thousands of petitions are presented each year in the various District Courts throughout the country for plans of arrangement under Chapter XI of the Bankruptcy Act.* If the contention of the Court below is to prevail, creditors would hesitate in making investigations to see whether or not fraud existed, or whether the plan was feasible or in the best interests of the creditors. If they had to wait until after a plan was approved and an application for confirmation filed and a deposit made under such plan, then very few, if any, creditors would ever file objections. The creditors who may wish to file objections would certainly not make preliminary investigations and incur large expenses, with

* A study of the Bankruptcy Records for the Southern District of N. Y. shows that during the fiscal year ending June 30, 1956, 804 petitions were filed (numbers 91,165-91,968), of which 105 embraced petitions under Chapter XI.

knowledge that their chances of being reimbursed, if successful, would be about nil. To wait until the last moment would be of no benefit, because at that time it would be too late to begin an investigation.

Far from being an "anomalous" situation, it is a normal situation for Congress to want to have the creditors with information leading to a refusal of a plan of arrangement make such investigations early in the proceedings.

3 Collier on Bankruptcy, p. 1547, agrees with this. In fact, *Collier* goes further and advocates that successful opposition to the *mere* offer of a plan should be compensated under Section 64a (3) of the Bankruptcy Act.

It is important that, in the public interest, this question be passed upon by this Court. If rights of objecting creditors are not fully protected then objections to a plan of arrangement by a creditor would be a rarity. It is not, as the Court below stated, "a gap to be bridged by judicial legislation." Section 64a (3) of the Act fully provides for the rights of these creditors.

4.

The decision of the Court below is believed to be erroneous. (a) It is in conflict with Congressional intent. (b) It emphasizes "form" over "substance", clearly overlooking the history of the proceedings. (c) It completely ignores that the debtor first tried to withdraw its plan *before* it stated to the Referee that it did not make a deposit. (d) There was a refusal here of the plan of arrangement, based on the merits of the objections of appellants. (e) It stresses an anomalous situation which, to the Referee who set the dates for the hearing, was a normal procedure, based on his experience as a referee. (f) It also ignores the fact that creditors do not wait until the last moment to make their investigations. Investigations must, of necessity, be made long before that time.

An objecting creditor who has incurred large expenses will thus be deprived of his matured rights. It would destroy the very purpose for which Sec. 64a(3) was enacted by Congress.

Conclusion

For the foregoing reasons, this petition for a Writ of Certiorari should be granted.

Respectfully submitted,

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SOLOMON NACHBAR,
Counsel for Petitioners.

Opinion of Court of Appeals

UNITED STATES COURT OF APPEALS

FOR THE SECOND CIRCUIT

No. 233—October Term, 1958.

(Argued April 9, 1959 Decided September 9, 1959.)

Docket No. 25357

RICHARD SHONGUT, JACOB SHONGUT, INC. and MITCHELL MOGAL,

Appellants,

—v.—

JULES GOLDEN,

Trustee-Respondent.

Before:

HINCKS, LUMBARD and WATERMAN,

Circuit Judges.

Appeals from orders of the referee in bankruptcy in a Chapter XI proceeding denying petitions of creditors for allowances for costs and expenses, the orders having been affirmed without opinion by the District Court for the Southern District of New York, Sugarman, *J. Affirmed.*

ABRAHAM J. GOLDBERG, New York, N. Y., *for Richard Shongut and Jacob Shongut, Inc., appellants.*

SOLOMON NACHBAR, New York, N. Y., *for Mitchell Mogal, appellant.*

GEORGE POLLACK, New York, N. Y. (Milton M. Eisenberg, Brooklyn, N. Y., on the brief), *for trustee-respondent.*

HINCKS, *Circuit Judge:*

The only question raised by this appeal is whether the referee in bankruptcy, whose order was confirmed without opinion by the court below, was correct in denying petitions for allowances for costs and expenses filed by three creditors under Section 64(a)(3) of the Bankruptcy Act, 11 U. S. C. A. § 104(a)(3). The facts are not in dispute and may be briefly stated.

On December 14, 1955, 116th Street Pawnbrokers, Inc., filed a petition for an arrangement under Chapter XI, Section 322, of the Bankruptcy Act, 11 U. S. C. A. § 722. On May 8, 1956, the referee held a hearing on the third amended plan, which was approved by a majority of creditors. Three creditors, the appellants here, opposed the plan; they were given two weeks to file specifications of objections to confirmation of the plan and the date for hearing of their objections was set for May 31, 1956. At the hearing, the debtor sought to withdraw the plan, but leave so to do was refused by the referee. The debtor then pointed out that the deposit required under Section 337(2) of the Act, 11 U. S. C. A. § 737(2), had not been made, and that an application to confirm the arrangement had not been filed within the time fixed by the court pursuant to Section 337(3), 11 U. S. C. A. § 737(3). Although the appellants were ready with their evidence in opposition to a confirmation, the referee refused to hear them and, without taking any evidence, for lack of the required deposit and application for confirmation declared the debtor bankrupt pursuant to Section 376 of the Act, 11 U. S. C. A. § 776. Thereafter these

appellants, under Section 64(a)(3) of the Act, 11 U. S. C. A. § 104,[1] made applications for allowances from the estate to cover fees and expenses of counsel who had been retained by them to oppose the confirmation of the plan and who had spent much time in the preparation of their opposition. On April 3, 1958, the referee dismissed these applications. The District Court affirmed the orders and these appeals followed.

In considering the appellants' contentions, we shall have in mind the general principles governing allowances to creditors for costs and expenses and in particular the principle that "the paramount postulate of economy pervading the law on bankruptcy liquidation requires that an omission by the legislator to provide for costs and expenses to creditors in a particular situation be construed as a purposed exclusion, not as a gap to be bridged by judicial legislation." 3 Collier on Bankruptcy, ¶ 62.21. See also *Saper* v. *Viviane & Son, Inc.*, 2 Cir., 258 F. 2d 826; *In re Friedman*, 2 Cir., 232 F. 2d 151, cert. denied *sub nom. Klein* v. *Brandt & Brandt Printers, Inc.*, 352 U. S. 835.

It is abundantly clear from the provisions of Section 64(a)(3), in so far as presently pertinent, that the costs and expenses of creditors in connection with a confirmation of arrangement may be allowed only "where the confirmation * * * has been refused * * * upon the objection and through the efforts" of creditors such as these appellants. Under Section 362 of the Act, the deposit required under Section 337(2) and a timely application for confirmation subsequent to the required acceptance of the plan, are conditions to confirmation. 8 Collier on Bankruptcy, ¶¶ 9.15, 9.16. In this case there had been no application for confirmation, no deposit, and the referee made no order

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[1] Bankruptcy Act, Section 64(a)(3), 11 U. S. C. A. § 104(a)(3), allows, as a debt having third priority:

"where the confirmation of an arrangement * * * has been refused, revoked, or set aside upon the objection and through the efforts and at the cost and expense of one or more creditors * * * the reasonable costs and expenses of such creditors in obtaining such refusal, revocation, or setting aside * * *"

either confirming or denying confirmation. With the proceedings in such posture, it is not permissible to argue that the confirmation was "refused" because of lack of application and deposit. For throughout the Act reference to a *refusal* of confirmation imports a refusal based on lack of merit in the plan in contradistinction from lack of the fulfillment of the several stated procedural conditions to confirmation. This is especially apparent in the provision of Section 376 which specifies that a refusal of confirmation is an independent ground for an order of adjudication in addition to the non-fulfillment of the stated conditions to the granting of a confirmation. The insistence of the appellants that "before the Referee could decide whether he would dismiss * * * or adjudicate * * * he was required to determine whether the specifications warranted a 'refusal' to confirm, or a confirmation" is plainly fallacious: it is in direct contravention to Section 376. It may be noted that under Chapter X, Section 236 of the Act, the concept of a *refusal* of confirmation is similarly limited.

The appellants argue that since a debtor, whose plan has been accepted, cannot withdraw his plan—cf. *In re Bryer*, 281 F. 812—he should not be allowed to "effectively thwart the opposition of a diligent creditor who opposes a confirmation of a plan by stating that he cannot make the deposit." It is hard for us to see how a debtor by failing to fulfill a condition to confirmation can be considered to have thwarted opposition to confirmation. If anything, it would seem to us that he had cooperated with opposition to confirmation by making confirmation legally impossible. Rather than having "thwarted" opposition he has obviated need for opposition.

The appellants further urge that it will defeat the policy of the Act if a debtor is allowed to wait until specifications of objections are filed and then, if he finds that the objections have merit, decide to withhold the required deposit. For under such a procedure, appellants say, "the objecting creditor who has incurred expense in investigation and

preparation would thus be at the mercy of the debtor. No creditor under such circumstances would risk incurring expenses of investigation." This argument overlooks the fact that under Section 337 of the Act it is for the referee to fix the time and place where the deposit shall be made, and a prudent creditor does not have to begin preparation of his objections to confirmation until the deposit has been actually made. Instead, he may press for compliance with the deposit provisions of Section 337. If then compliance is not forthcoming, time-consuming preparation will be unnecessary, for adjudication or dismissal will summarily follow. If, however, the deposit is made, it will be time enough then for the creditor to proceed with his preparations.

It is true that the situation below seems to have been anomalous in that the referee set a date for a hearing on a confirmation of the plan before an application for confirmation had been made. We assume this was done on the chance that the proceedings might thereby be expedited. But in this respect also, a creditor intending to incur expense in preparation of opposition could have pressed the referee to set a limit on the time within which the debtor might apply for confirmation and to set the hearing at a reasonable time thereafter in order to permit suitable preparation for the hearing. Not having taken such action, these appellants are in no position to claim prejudice from the anomalous procedure. And certainly, the intrusion of an occasional anomaly into the proceedings is not sufficient ground for overriding the limitation of Section 64(a)(3) on allowances to creditors.

Since therefore there has been in this case no refusal of a confirmation, we hold the denial of the allowances sought by these appellants was plainly required under Section 64 of the Act. And we think that in the situation which underlies this appeal the denial of allowances to these appellants who incurred expense to oppose a confirmation before confirmation had been sought, operated not at all to defeat the objectives or the spirit of the Act.

Affirmed.

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In the Matter

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Bankrupt.

RICHARD SHONGUT, JACOB SHONGUT, INC., and MITCHELL MOGAL,

Petitioners-Appellants,

JULES GOLDEN,

Trustee-Respondent.

TRUSTEE-RESPONDENT'S BRIEF IN OPPOSITION TO A PETITION FOR A WRIT OF CERTIORARI BY THE PETITIONERS-APPELLANTS

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Trustee-Respondent.

TRUSTEE-RESPONDENT'S BRIEF IN OPPOSITION TO A PETITION FOR A WRIT OF CERTIORARI BY THE PETITIONERS-APPELLANTS

The facts as briefly and fully stated in the opinion by the United States Circuit Court of Appeals are as follows:

On December 14, 1955, 116th Street Pawnbrokers, Inc. filed a petition for an arrangement under Chapter XI, Section 322, of the Bankruptcy Act, 11 U. S. C. A. Sec. 722. On May 8, 1956, the referee held a hearing on the third amended plan, which was approved by a majority of creditors. Three creditors, the appellants here, opposed the plan; they were given two weeks to file specifications of objections to confirmation of the plan and the date for hearing of their objections was set for May 31, 1956. At the hearing, the debtor sought to withdraw the plan, but leave so to do was

refused by the referee. The debtor then pointed out that the deposit required under Section 337(2) of the Act, 11 U. S. C. A. Sec. 737(2), had not been made, and that an application to confirm the arrangement had not been filed within the time fixed by the court pursuant to Section 337(3), 11 U. S. C. A. Sec. 737(3). Although the appellants were ready with their evidence in opposition to a confirmation, the referee refused to hear them and, without taking any evidence, for lack of the required deposit and application for confirmation declared the debtor bankrupt pursuant to Section 376 of the Act, 11 U. S. C. A. Sec. 776. Thereafter these appellants, under Section 64(a)(3) of the Act, 11 U. S. C. A. Sec. 104, made applications for allowances from the estate to cover fees and expenses of counsel who had been retained by them to oppose the confirmation of the plan and who had spent much time in the preparation of their opposition. On April 3, 1958, the referee dismissed these applications. The District Court affirmed the orders and appeals followed.

The sole issue involved is whether there was a "refusal" upon the merits of a plan of arrangement within the purview and meaning of Section 64(a)(3) of the Bankruptcy Act, 11 U. S. C. A. Sec. 104(a)(3), and whether that "refusal" was due to the objections, efforts and at the cost and expense of the opposing creditors.

The relevant portion of the statute involved is as follows:

> "Bankruptcy Act, Section 64(a)(3), 11 U. S. C. A. Sec. 104(a)(3), allows, as a debt having third priority:
>
> > 'Where the confirmation of an arrangement * * * has been refused, revoked, or set aside upon the objection and through the efforts and at the cost and expense of one or more creditors * * * the reasonable costs and expenses of such creditors in obtaining such refusal, revocation, or setting aside * * *.'"

In the subject case there was an adjudication by the referee as a result of the nonfulfillment of stated procedural conditions to confirmation including among other grounds, a lack of deposit. There was no refusal of confirmation based upon a lack of merit in the plan or based upon the objection and through the efforts of the appellants-creditors.

The petitioner contends that the issue involved is of sufficient general application beyond the interest of the parties to this proceeding and that it presents a question of great importance allegedly affecting the very substance of bankruptcy proceedings and objecting creditors.

Actually what is involved in this case is that the appellants-creditors proceeded with their investigation and services in connection with objections which were filed before the fulfillment of certain stated procedural conditions to confirmation.

If the appellants had waited as indicated by the Circuit Court of Appeals, until the deposit had been actually made before preparing the objections to confirmation, then all of the efforts and objections of the appellants would have been avoided.

The appellants argue in effect as a matter of equity and fairness that they are entitled to consideration since they were diligent in conducting an investigation and preparing objections and that therefore they should be compensated for the same, even though no hearing was ever had. Whether the objections or services of the creditors involved herein had any merit whatsoever, remains completely undetermined, since no hearing was ever held.

The provisions of the statute involved, namely Section 64(a), subdivision (3), of the Bankruptcy Act, are clear and the interpretation to be applied to the act as well as the application of equitable principles to the issues has been fully and completely determined by prior judicial decisions.

In the case of *In re Friedman*, 2 Cir., 232 F. 2d 151, cert. den. sub nom. *Klein* v. *Brandt and Brandt Printers, Inc.*, 352 U. S. 835, it was stated on page 152:

> "it is well settled that the bankruptcy court lacks power to grant, and the policy of the act is against, compensation not expressly provided for by the act. Lane v. Haytion Corp., 2 Cir., 117 F. 2d 216, 219, cert. den. 313 U. S. 580, 61 S. Ct. 1101, 85 L. Ed. 1537.
>
> "Although it has been broadly stated that a bankruptcy court is a court of equity, Young v. Higbee Co., 324 U. S. 204, 214, 65 S. Ct. 594, 89 L. Ed. 890, the exercise of t' s equitable power must be strictly confined withir the prescribed limits of the Bankruptcy Act. See Berry v. Root, 5 Cir., 148 F. 2d 945, 946, cert. den. 326 U. S. 755, 66 S. Ct. 91, 90 L. Ed. 453.
>
> "Where Congress intended that allowances should be made, it has carefully enumerated them and any omission must be construed as express exclusions. 3 Collier, Bankruptcy 534-7 (14 Ed.)."

The Circuit Court of Appeals in the case at bar, therefore, correctly stated in reviewing the general principles governing allowances of creditors "the paramount postulate of economy pervading the law on bankruptcy liquidation requires that an omission by the legislator to provide for costs and expenses to creditors in a particular situation be construed as a purposed exclusion, not as a gap to be bridged by judicial legislation."

It is therefore certain that the creditors can receive compensation where there has been a refusal upon the merits and due to the objections and through the efforts of the creditors. Although in subdivision 1, page 10 of the petition, the appellants argue that the refusal to confirm was based on the merits of the case and not on the nonfulfillment of the procedural conditions, the appellants fail to set forth in what

respect the alleged refusal was based upon the merits of the case.

The sole conclusory and improper argument is made that "refusal" may be in various forms and may be inferred from the circumstances surrounding the proceedings.

The argument is then made by the appellants that the debtor in some way knew that the objections of the creditors would be sustained and therefore failed to put forth a deposit. This is pure conjecture and surmise and the appellants might as well contend that the referee by some miracle could know or infer that there was merit to the objections by the creditors upon which no hearing had been held.

It is submitted that a strict interpretation of the statute is necessary since to do otherwise would be to open up the door to claims for fees based merely upon the fact that objections were filed. In addition a loose interpretation would permit post-mortem speculations as to the possible effect a filed objection had upon a turn of events even though no proof was ever presented in connection with the objections.

The appellants' entire position is based upon pure speculation that they could have proved fraud if permitted by the referee and whatever proof they could have offered would have resulted in a refusal on the merits by the referee thus giving rise to a basis for their application for expenses and fees. As a result there was no refusal on the merits of the case and to infer that the referee by adjudicating the debtor as a bankrupt, as a result of non-compliance with procedural requirements, was making a determination upon the merits, would constitute crystal ball gazing but not an inference based upon any facts.

Under subdivision 2, the appellants argue in essence that the referee erred in not conducting a hearing on the objections and that in effect the referee's adjudication of bankruptcy was in error.

It must be pointed out that there was no appeal from the order of adjudication which in effect precluded the

appellants from having a hearing on the objections and therefore the contention of the appellants under then subdivision 2 of the petition does not properly lie. Since no appeal from the order which precluded a hearing was filed, the claim that a hearing should have been held by the referee cannot be maintained.

The appellants contend, however, that the case of *Meyers* v. *Intl. Trust Co.*, 263 U. S. 64, 72, held that a reference for a hearing of objections is equivalent to a hearing in equity and constitutes a new suit.

The respondent believes that the authority of *Meyers* v. *Intl. Trust Co.*, 263 U. S. 64, 72, does not apply in any manner whatsoever to the case at bar. In addition, any interpretation that the filing of objections is equivalent to the start of a new suit and a hearing in equity does not foreclose a determination or dismissal of that suit on justifiable grounds for which the objecting creditor was in no way responsible.

The appellants' authorities to the effect that a debtor cannot withdraw a plan as a matter of right, have no application to the facts involved in the case at bar since no withdrawal by the debtor was permitted by the referee.

Under subdivision 3 of the petition the appellants contend that the question involved is of great importance in the administration of the Bankruptcy Act since thousands of petitions are presented each year for plans of arrangement and that creditors would very rarely file objections if they had to wait until an application for confirmation was filed and a deposit made.

It is a matter of common knowledge that objections are not rare and that the provisions of Section 64(a)(3) fully provide for the rights of all those creditors, as admitted by the appellants.

The appellants quote Collier on Bankruptcy as advocating the suggestion that successful opposition to the mere offer of a plan should be compensated.

The appellants then incorrectly quote the court below and try to attribute to the court below the opinion that the problem as presented by the appellants is "a gap to be bridged by judicial legislation."

An examination of the opinion in the court below indicates that the complete and correct quotation as set forth on page 17 of the petition is as follows:

> "The paramount postulate of economy pervading the law on bankruptcy liquidation requires that an omission by the legislator to provide for costs and expenses to creditors in a particular situation be construed as a purposed exclusion, not as a gap to be bridged by judicial legislation."

It is therefore clear that the Circuit Court of Appeals did not describe this issue or problem "as a gap to be bridged by judicial legislation" but rather that the omission of the statute to provide for any particular situation was not a gap to be bridged by judicial legislation. There is no evidence that the rights of objecting creditors are not fully protected by the statute and that certainly objections to a plan of arrangement are not a rarity as contended by the appellants.

It is respectfully submitted that the statute involved is clear and presents no confusion. It provides with good reason, that only an objecting creditor who succeeds on the merits in proving his objection and thus bringing about a refusal of a plan of arrangement, can be compensated for his efforts. The principles of law involved have been thoroughly adjudicated and firmly established.

This case merely involves creditors who took it upon themselves to perform certain services at a time when those services could have been held in abeyance, if the rules had been followed by the appellants-creditors.

The case does not involve an issue which would be applicable to all other objecting creditors and therefore this case is not a proper one for review by certiorari in this court and the petition for a writ of certiorari should be denied.

Respectfully submitted,

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